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RIGHT OF THE TAXPAYER IN COMPUTING HIS NET INCOME UNDER THE INCOME TAX ACT TO DEDUCT LOSS SUSTAINED IN SPECULATION OUTSIDE OF HIS REGULAR BUSINESS.—The interesting question as to whether loss sustained in speculation outside of the taxpayer's regular business is deductible under the Income Tax Act was recently before the United States District Court for the Southern District of New York in the case of *Mente v. Eisner*, 266 Fed. 161. The court held that deductions under the Income Tax Act of Oct. 3, 1913, § II, subd. 2B are limited to losses incurred in the actual business of the taxpayer, as distinguished from isolated transactions, and do not include losses sustained through dealing on an exchange by one engaged in another regular business.

The Income Tax Act of 1913, in setting forth the deductions allowed in computing net incomes, provides:¹

"* * * Fourth, losses actually sustained during the year, *incurred in trade* or arising from fires, storms, or shipwreck, and not compensated for by insurance or otherwise."
(Italics supplied.)

¹ Income Tax Act of Oct. 3, 1913, § 11, subd. 2B (38 Stat. 167).

Within the meaning of this provision, what are losses "incurred in trade"? Unquestionably, losses directly connected with, or arising out of, the particular line of trade in which the taxpayer is engaged are deductible. They include losses by fire,¹ burglary,² embezzlement,³ shipwreck¹ or tornado,¹ so long as the person suffering the loss is not protected therefrom by insurance or otherwise. But do they include losses incurred by speculation with the funds secured from the income received by the taxpayer from some other line of business? The English Income Tax Act covers the point by specifically providing:⁴

"No deduction is to be made * * * for loss not connected with or arising out of (in the sense that it is really incidental to) the trade." (Parenthetical matter supplied.)

Due to the ambiguity in the meaning of "incurred in trade", it is necessary to interpret the legislative intent of Congress in incorporating that phrase into the body of the act.

In a popular sense, "trade" comprehends every species of exchange or dealing.⁵ It is defined by Bouvier as "any sort of dealings by way of sale or exchange".⁶ "Trade" in its broadest signification includes not only the business of exchanging commodities by barter, but that of buying and selling for money, or commerce and traffic generally.⁷ Under this interpretation, any person might be brought within the act as a trader who bought and sold for gain, though his dealings might be on a very small scale compared with his means invested in other ways, or might be isolated transactions remote from his regular occupation. In contrast to the ordinary use and acceptance of the term "trade", there is a technical legal meaning not admitting of precise definition, but which yields to exemplification.

The strict constructions of the word "trader" in the English and American Bankruptcy Acts are propositions analogous to the one at hand. To prevent litigation, the English have prescribed a long list of occupations and transactions which ordinarily would not be considered under the title of "trades", but which are so considered by virtue of the technical legal meaning of the term as used in the statute. The courts in this country have been forced to attack the question in a different manner by judicially eliminating from the purview of the statute occupations and transactions which do not rightfully come under the title of "trade". Thus, our courts in construing the technical legal meaning of "trade" under the Bankruptcy Act, have held: that dealings limited to the products of one's own land do not consti-

² BLACK, INCOME TAXES, § 99.

³ *United States v. Central National Bank*, 10 Fed. 612.

⁴ 16 THE LAWS OF ENGLAND, § 1310 (Income Tax Act, 1842, s. 100).

⁵ *In re Surety Guarantee & Trust Company*, 121 Fed. 73.

⁶ 3 BOUVIER, LAW DICTIONARY, Rawle's 3rd. ed., 3290.

⁷ *May v. Sloan*, 101 U. S. 231; *United States v. Douglas*, 190 Fed. 482.

tute trading;⁸ that one who contracts with a railroad company to grade and build its road is not a trader;⁹ that the occasional trading of a farmer in horses may make him a trader in common parlance, but he is not a tradesman under the technical meaning of the term;¹⁰ that a theatrical manager who occasionally bought and sold costumes is not a tradesman;¹¹ that a teamster, who, even to a very considerable extent, buys and sells hay for the *bona fide* purpose of keeping his team from standing idle is not a trader;¹² that a mining company is not a corporation engaged in trade;¹³ that an insurance company is not engaged in trade;¹⁴ and that one who speculates in stocks is not engaged in trade, for in the occupation of buying and selling shares of stock on speculation, the element essential to the technical legal meaning of "trade" is lacking, namely, goods, wares, or merchandise.¹⁵ If these analogies are applied, the taxpayer in the instant case is not engaged in trade and therefore he is not entitled to deduct loss resulting from speculation in cotton futures.

In the Income Tax Act of 1913, did Congress employ the term "trade" in its broadest signification or in the technical sense known to the law? The fact that the act makes gains and profits derived from *any source* whatsoever part of the taxable income leads to a strong presumption that Congress intended losses sustained from like transactions to be classified under "allowed deductions" in ascertaining the net taxable incomes. The Treasury Department, in administering the act, interprets "in trade" as being synonymous with *business*,¹⁶ which, *taken by itself*, can be viewed upon principle in no other light than the use of "trade" in its usual and broadest signification. However, whatever may have been the intention of Congress in the use of the word "trade", it is plain that the Treasury Department has construed it in its technical legal meaning, as evidenced from the following appurtenant decisions:

"Losses * * * will not be deductible at all unless they are incident to, connected with, or grow out of the *business* of the individual or corporation sustaining the loss * * *." ¹⁷

"The doing of a single act incidentally or of necessity not pertaining to the particular business of the person doing the same will not be considered engaged in or carrying on the business." ¹⁸

⁸ *In re Woods*, 30 Fed. Cas. 529.

⁹ *In re Smith*, 22 Fed. Cas. 394.

¹⁰ *In re Cote*, 6 Fed. Cas. 614.

¹¹ *In re Duff*, 4 Fed. 519.

¹² *In re Kimball*, 7 Fed. 461.

¹³ *In re Elk Park Mining & Milling Company*, 101 Fed. 422.

¹⁴ *In re Cameron, etc., Insurance Company*, 96 Fed. 756.

¹⁵ *In re Marston*, 16 Fed. Cas. 857; *In re Woodward*, 30 Fed. Cas. 542.

¹⁶ Treasury Department Decision No. 1989.

¹⁷ Treasury Department Decision No. 2005.

¹⁸ Treasury Department Decision No. 1989.

"As to losses on stocks, grains, cotton, etc., if these are incurred by a person engaged in trade, to which the buying and selling of stocks, etc., are incident as a part of the business, as by a member of a stock, grain, or cotton exchange, such losses may be deducted."¹⁹

In these decisions, the Treasury Department has used "business" and "trade" as correlative terms, but the interpretation placed upon them is "*his business*", thereby denying the broad signification of the term and adopting the restricted legal meaning. The court in the instant case upheld these decisions as correctly construing the legislative intent of Congress.²⁰

The decision in the instant case was made in total disregard of new light shed upon the legislative intent of Congress in the use of the term "trade" by recent amendments to the Income Tax Act. Congress, evidently awakened to a realization of the ambiguity of the term "trade", put to rest any doubt there may have been as to its legislative intent by inserting in the section of the original act dealing with allowed deductions in computing net incomes the following provision:²¹

"* * * Losses sustained during the taxable year and not compensated for by insurance or otherwise, if incurred in *any transaction entered into for profit, though not connected with the trade or business*; * * *." (Italics supplied.)

Whether this amendment to the Income Tax Act is declaratory of the intention of Congress that the term "trade" be construed in its broadest signification is now immaterial. It is enough that this amendment is positive law, and the failure of the court in the instant case to allow the taxpayer, in computing his taxable income, to deduct losses actually sustained through transactions entered into for profit, though not connected with his regular business, is in distinct derogation of the law.

F. S. T., JR.

ARE STOCK DIVIDENDS INCOME?—The Sixteenth Amendment to the Constitution of the United States provides that Congress shall have power to lay and collect taxes on incomes, from whatever source derived, without apportionment among the several States, and without regard to any census or enumeration. In pursuance of this Amendment, Congress enacted that stock div-

¹⁹ Treasury Department Decision No. 2090.

²⁰ *Mente v. Eisner, supra*. It is to be regretted that, in framing a statutory provision of as much importance as the Income Tax Act, a term so vague and admitting of such variety of signification has been employed.

²¹ Federal Revenue Act of 1918, approved Feb. 24, 1919, Title II, Part II, § 214, subd. 5. U. S. Comp. St. Supp. 1919, § 6336 $\frac{1}{2}$ g.